

5 November 1968

MEMORANDUM FOR THE RECORD

SUBJECT: American Management Association Orientation Seminar #1236-05 - Financial Management of the Corporate Pension Fund

1. The undersigned attended the subject Seminar during the period October 16 through October 18, 1968 at AMA's New York headquarters. Details on the material covered are contained in the AMA binder provided to all registrants which will be maintained in our office library. However, it was felt a memorandum should be written to highlight a few significant points which may have applicability to our [REDACTED] and probably even more importantly to the Insurance Complex Investment Portfolio.

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2. First, it should be emphasized that the entire Seminar was devoted, as the subject indicates, to the investment and financial management of corporate pension funds and did not cover pension benefits as such. Also, the program was principally geared towards large corporations and financial institutions involving funds in the \$100 million to \$500 million category. However, with this caveat, it still appears that there are some investment criteria that have applicability to us.

3. While most pension funds are still being actuarially calculated at the 4-1/2 per cent interest rate, the funds themselves are actually earning substantially more through equity investments. Twenty-five years ago almost all pension funds were in corporate and government bonds. Now at least 50 per cent of the funds are in common stocks. Most pension funds are managed by the trust departments of banks and to a lesser extent by insurance companies. However, this may be because it is only within the last five to six years that insurance companies have been authorized to operate pooled investment funds. While most companies are not actually managing their own funds, there appears to be at least a small trend in that direction. General

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Tire and Rubber Company self-administers their own pension funds and their fund manager spoke at the Seminar. He gave a presentation on both the advantages and disadvantages of this procedure. The self-administered Goodyear Portfolio has averaged a 25 per cent per year rise during the last five years. It was his conclusion that if the fund is in the \$25 million to \$50 million range, self-administration should be considered. Since this is definitely out of our range, I will limit my comments to the standards and criteria given for rating performance by outside fund managers or investment counselors.

4. A few of the speakers recommended more than one investment advisor or manager on the theory that competition improves performance. However, all of the speakers were talking about very large funds which could be sliced up in numerous substantial portions. It was the consensus of all speakers that it takes approximately three to five years to evaluate the performance of the investment advisor. It was also strongly emphasized that once the advisor is given the objective of the fund and any appropriate investment restrictions, he should be given complete discretion as to how the fund was invested. An advisor cannot be rated on decisions that are not his own. It also was the consensus of the speakers that for efficient fund management the optimum amount is \$100 million to \$300 million. Beyond that the fund does not have the flexibility of getting in and out of the Market without a real impact. It was therefore recommended that for those companies placing their funds with banking institutions and insurance companies, that they not permit their funds to be placed in a pooled arrangement that goes over this maximum.

5. Considerable time was spent in the Seminar on performance measurement of advisors/fund managers. It was generally agreed that comparison should be made with the Standard & Poor's Select 500 instead of the Dow Jones Average since the SP generally beats Dow by 1 per cent. (In rating they all add dividend income to capital appreciation and make a market to market comparison.) The investment officer of AETNA Life said it was their target to get a return of two-thirds or 6 per cent more, whichever is higher, than the SP. The investment officer from the Wells Fargo Bank categorized funds by objectives and risk levels. On a fund with maximum income objectives, he felt that 6 to 7 per cent return should be realized. On a fund where income is the primary objective and capital

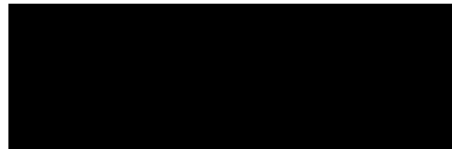
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appreciation only a secondary consideration, the return should be 8 per cent. On a balanced income/growth fund, the income return should be in the 4 to 5 per cent bracket and the growth should be 10 per cent. On a growth fund, the income return should be 2 to 3-1/2 per cent and the growth should be 12 per cent. On a maximum growth fund, the interest return should be 1-1/2 per cent to 2 per cent and the appreciation, 14 per cent. (All of these figures represent the return that should be anticipated annually and computed annually.)

6. It was also the Wells Fargo man's position that an equity portfolio should be divided approximately fifty-fifty between what he categorized as strong basic holdings and opportunistic holdings. For him, basic holdings must have very sound management, above average growth and be either technically or consumer service oriented. The basic holdings should be kept for the long-haul growth. Opportunistic holdings are made in "turn-around" companies and companies which are changing character of their operations. The opportunistic holdings should realize a 30 per cent appreciation per year. Wells Fargo, in its portfolio selection, operates against named securities; whereas in contrast, AETNA establishes the criteria for the stock it wants and then runs it through its computer to get a stock that fits the criteria. It was also the consensus of all the speakers that no one fund manager should be charged with responsibility for more than 35 to 40 different issues. In fact, if anything, that number may be somewhat high and they were all talking about very large portfolios. For example, Goodyear has 2/3 of its over \$100 million portfolio in 29 issues and the remaining 1/3 in 50 issues which they feel is much too many. Everyone preached that concentration was much better than wide-spread diversification. If the fund manager/advisor has too many issues to watch, none can be watched effectively. All the managers rely heavily on Wall Street research and, I believe, inside information. Commissions are their leverage to get the best information. It was the opinion of most of the speakers that while some mutual funds have had spectacular record, most of them suffer from the lack of consistency in performance. While they recognize that a good mutual fund may well deserve a place in the pension fund portfolio, they warn against most of the go-go funds and the too big funds.

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7. During the final round-up with the Chairman, as a rule of thumb guidance for judging pension portfolio performance, he felt that if the portfolio was performing 2 per cent more than the SP 500 with 1/3 more risk than the Market and that the manager/advisor was performing at 80 per cent consistency, it was a good portfolio.



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